



State Administration, Public Retirement, and Veterans' Affairs Interim Committee

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56th Montana Legislature

SENATE MEMBERS

SUE BARTLETT, VICE-CHAIR
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GLENN A. ROUSH

HOUSE MEMBERS

MATT BRAINARD, CHAIRMAN
EDITH J. CLARK
TOM DELL
CAROL WILLIAMS

COMMITTEE STAFF

SHERI HEFFELFINGER
RESEARCH ANALYST
JOHN MacMASTER, ATTORNEY
DAVID NISS, ATTORNEY
JOANN JONES, SECRETARY

MINUTES

DISABILITY AND RETIREE HEALTH CARE SUBCOMMITTEE

AUGUST 3, 2000
CAPITOL BUILDING
HELENA, MONTANA

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed. Committee tapes are on file in the offices of the Legislative Services Division. **Exhibits for this meeting are available upon request. Legislative Council policy requires a charge of 15 cents a page for copies of documents.**

COMMITTEE MEMBERS PRESENT

Sen. E.P. "Pete" Ekegren, Chairman
Sen. Sue Bartlett
Sen. Glenn A. Roush

Rep. Matt Brainard
Rep. Tom Dell

STAFF PRESENT

Sheri Heffelfinger, Research Analyst
David Niss, Attorney
Jo Ann Jones, Secretary

VISITORS

Visitors' list, Attachment #1.

COMMITTEE ACTION

- C Agreed to strike subsections 2 and 3 of LCDISA, to replace those sections with instructions to the PERB to construct a disability plan for vested DC plan

members, to develop alternative terminology for the 0.43% contribution, and to specify that repayment of any loans obtained to fund disability coverage for DC plan members cannot be taken from the DB trust fund.

- C Agreed to clarify ambiguous terminology in LCVEBA in regard to the 25% limit on contributions of unused sick leave to a health care trust account
- C Instructed staff to write an Issues and Options Paper for presentation to the Subcommittee to outline the unresolved issues about LCVEBA

CALL TO ORDER AND ROLL CALL

Sen. Ekegren called the meeting to order at 8:10 a.m. Roll call was noted; see Attachment #2.

Sen. Bartlett moved adoption of the minutes as distributed; seconded by Rep. Brainard. The motion was passed unanimously by voice vote.

DISABILITY COVERAGE FOR DEFINED CONTRIBUTION PLAN PARTICIPANTS

Exhibit #1: LCDISA

David Niss, Committee counsel, said Section 1 of LCDISA requires the Public Employees Retirement Board (PERB) to offer a disability benefit to vested Defined Contribution (DC) plan members by either purchasing insurance or by offering a self-insured plan. The PERB determines whether a disability has occurred and to what extent. The benefit may be paid only until the disabled participant turns age 60. A Defined Benefit (DB) plan member who transfers to the DC plan shall be covered by disability coverage just as if the election for the DC plan had not taken place.

Mr. Niss said the rest of the bill, except for Section 4 on page 7, amends existing law in order to implement the disability coverage in Section 1. Section 4 authorizes the PERB to accept a loan from the Board of Investments to cover disabilities that may occur right after plan startup.

Rep. Brainard asked if LCDISA, in its final form, should not pass the 2001 legislation session, would the disability coverage provided in HB 79, although not specifically

stated therein, still be a contractual right. Mr. Niss said yes, the concept of LCDISA is codified from the provisions of HB 79.

Sen. Bartlett said that according to HB 79, a member who chooses to leave the DB plan for the DC plan, having received all the required information about the DC plan package, is electing to give up a contractual right to disability coverage.

Rep. Brainard said that Section 2 appears to be murky in that 0.43% of the compensation must be added to the plan choice rate for the purpose of funding a disability benefit. He said that some of the confusion may lie in the fact that the bill does not spell out how a disability benefit is determined. Ms. Heffelfinger said the decision had been made by the Subcommittee to give DC plan members the same benefit that is currently given to DB plan members. Rep. Brainard said the language providing the DC plan member *at least* the same benefit given now in the DB plan is not necessary. Ms. Heffelfinger said that, currently, disability coverage is tiered and the bill provides the third tier of coverage. Rep. Brainard asked which tier provides the best coverage. Mike O'Connor, Executive Director, PERB, said that it depends on the member's years of service. Rep. Brainard asked if a DB plan member who now has the lowest tier of disability coverage would be better protected if transfer would be made to the DC plan. Mr. Niss said whatever coverage a DB plan participant receives now would be protected if transfer is made to the DC plan. Mr. O'Connor said there will be a 2-tier system of disability coverage in the DC plan after it is implemented because the PERB will determine disability coverage for new hires.

Rep. Brainard said that he had envisioned disability coverage to be determined by a standard formula.

Sen. Bartlett said it might be wise to drop subsections (2) and (3) of section 1 and handle disability coverage as an entirely new plan. She said that she did not like to knowingly establish tiers of coverage, so it might be better to state that the PERB will

establish disability coverage for DC plan participants and ignore whether the plan member is an existing employee or a new hire.

David Senn, Executive Director, Teachers Retirement Systems (TRS), said IRS rules require that benefits be paid until the age when full retirement can be taken. For DC plan members, their account would zero out at age 60.

Rep. Brainard said the intention is not to withdraw from members' DC plan accounts, but rather to establish a fund, similar to disability coverage in the DB plan. He said that a 58-year-old employee who is so close to retirement would be acting foolishly to elect a transfer to the DC plan. The education component should make that point obvious to most people. He said there is a necessity to establish some parity among employees in regard to disability benefits, and said that he does not like tiering of benefits, either.

Sen. Bartlett asked for clarification on the DC plan trust fund for disability coverage. Mr. O'Connor said that it would be a separate fund that would be invested and managed, disability benefit payments would come from that fund and would cease at age 60 when the participant would begin to rely on retirement benefits from the DC plan account.

Rep. Brainard said there could be only one pool as long as the contributions would pay the actuarial costs. Mr. O'Connor said the pool of money would essentially be a mini-DB plan. He said that if the contribution costs fluctuate regularly, then the trust fund would no longer be a DC plan because the contribution rate is not defined. He said the question is then whether it would meet IRS qualification rules.

Sen. Bartlett said a trust fund for disability benefits could be created where everyone contributes 0.43% whether they are DB or DC plan participants. Establishing a separate trust fund for DC plan disability coverage is a concern because its structure is unknown and the contribution rate might have to be increased.

Rep. Brainard said he would like the disability coverage to be a separate benefit from the retirement benefit.

Mr. Senn asked how this benefit would be structured for University system employees who chose TIAA-CREF but are still under PERS. Rep. Brainard said the retirement benefits provided by the insurance company and the PERS are offset. This benefit would not be prorated or offset.

Mr. O'Connor said the bill as written provides coverage for those people who elect TIAA-CREF.

Sen. Bartlett asked what types of problems might be encountered if a trust fund is created that includes contributions from all PERS employees no matter what their plan choice. Mr. O'Connor said the fluctuations would be smoothed out but there will be complaints from DC plan participants who want the contributions for investment purposes because they will perceive it as supplementation of the DB plan.

Rep. Brainard said that because it's all part of the same system, it would be within legislative prerogative to establish parity for all employees.

Sen. Bartlett asked if it is Subcommittee consensus to draft a bill to establish a pool for everyone in the PERS, with an exception for those in the University system who elect the Optional Retirement Plan (ORP).

Sen. Ekegren suggested that Mr. Niss continue with the summation of the bill, then the Subcommittee members can discuss it section by section.

COMMITTEE DISCUSSION OF LCDISA

Mr. Niss said that he was leery of establishing one trust fund for both DB and DC plans unless one plan is specifically prohibited from supporting the other.

Rep. Brainard said he did not understand how a person could end up with a lesser benefit than another person if all benefits are drawn from a common pool. He said that the PERB has already been given great flexibility, so that flexibility could be extended to disability coverage, too. He said that HB 79 authorizes the PERB to adjust the plan choice rate, if necessary.

Mr. Niss said he did not know whether reduced contributions would result in a lesser benefit.

Sen. Bartlett said that disability coverage cannot be provided for DC plan members from the DB trust fund. It would have to be a separate fund, not identified with either the DB or the DC plan. She said that's why the disability coverage contribution rate should not be part of the plan choice rate.

Sheri Heffelfinger, Research Analyst, asked whether the disability benefit is considered part of the DB plan's normal cost. If disability coverage is not considered part of the DB plan normal cost, then disability can be separated from the DC plan choice rate and then a pool that is separate from the retirement system can be created.

Rep. Brainard said he believes that it is possible to determine a rate for disability coverage separate from the plan choice rate, but that the PERB would have to be consulted.

Rep. Brainard said he recalled Subcommittee discussion to create separate DC plan disability coverage. Ms. Heffelfinger said the crux of the problem is whether the disability coverage portion of the DB plan is a contractual right. She said that neither

she nor David can answer that question without outside legal and tax help, so that is why the bill was drafted as it is.

Rep. Brainard said if an employee wants disability coverage, then the DB plan should be elected. But if there is going to be separate DC plan disability coverage, then the formula that is used should be the one that is used now. Ms. Heffelfinger said the Subcommittee decision was to use $1/56 \times \text{FAS} \times \text{years of service}$. She said the bill draft can be rewritten so that the final sentence of subsection 3 reads that there will be a disability benefit calculated through use of the formula set out in 19-3-108, MCA. She said the contribution rate for disability coverage in the DC plan was included in the plan choice rate so that it would be adjustable.

Sen. Bartlett said her preference is to strike subsections 2 and 3, and replace them with instructions to the PERB to construct disability coverage using the formula determined by the Subcommittee. She said that if disability coverage is left as a separate DC plan only, the contribution rate may rise higher than can be anticipated because the risk is spread across a smaller population.

Rep. Brainard said one of the drawbacks to the DC plan was the anticipation that younger, healthier people would migrate to the new plan, adversely affecting the DB plan, but only experience will determine what actually will happen.

Sen. Bartlett asked for comment on her suggestion to strike subsections 2 and 3.

Rep. Brainard said he agreed with Sen. Bartlett because it is a simplification and it does not differentiate between the two plans.

Rep. Dell asked if the PERB would have the leeway to lower the contribution rate if it turned out to be too high. Sen. Bartlett said that flexibility is allowed by Section 2. She said there is a possibility of forcing people into a lesser benefit through use of a

formula. Rep. Brainard commented that long-term DB plan members who choose to transfer to the new plan would not lose any disability benefits.

Mr. Niss said he understood that Rep. Brainard's concept involves the theory of informed choice and under that theory an employee would make a choice whether to abandon the benefits of a former contract for the benefits of a different contract. However, he said that whether this theory applies to a retirement benefit has not yet been determined by the courts.

Rep. Brainard said that in the event an issue about choice should reach the Montana Supreme Court, he hopes that the Court will consider the CPERS minutes from last interim where it is made clear that employees wanted to make choices for themselves. He said that an employee who chooses to transfer to the new DC plan is choosing to leave behind everything that is in the DB plan.

Ms. Heffelfinger said that Montana is not without precedent in offering optional retirement plans and asked Mr. Senn if there had been problems when University faculty lost disability coverage when choosing the ORP. Mr. Senn said no, but added that disability coverage was optional for the first three years, but is now mandatory for all ORP members.

Sen. Bartlett requested that staff examine whether specific mention need be made about employees who elect the ORP.

Sen. Ekegren asked if there were objections to the recommended changes to LCDISA. There were none, so he instructed staff to make those changes.

Sen. Bartlett said Mr. O'Connor might have concerns about the plan choice rate. Mr. O'Connor said the PERB tax counsel is examining whether the fluctuation of the plan choice rate would meet IRS qualifications.

Sen. Bartlett said the plan choice rate is charged to the DC members to keep the plan whole. She said creating the choice also creates an obligation to the DB plan. She said the 0.43% rate is to fund the disability coverage and she is not sure that it should be considered part of the plan choice rate.

Rep. Brainard asked if she would prefer to coin another term for the 0.43% and then allow the PERB to adjust it as required. Mr. O'Connor said he thought that suggestion would make explanation to plan members much easier.

Sen. Bartlett asked if the bill needs to state that repayment of any loan cannot be with funds drawn from the DB trust fund. Mr. O'Connor said he thought that would be necessary.

Rep. Brainard moved to adopt LCDISA, as amended; Rep. Dell seconded.

Mr. O'Connor distributed copies of **Exhibit #2: Public Employee Retirement Administration DC Plan Disability Issues and Decision Points.**

The motion passed unanimously by voice vote.

CREATION OF HEALTH CARE TRUST ACCOUNTS

Exhibit #3: LCVEBA

Exhibit #4: Public Employment Retirement Administration VEBA Issues and Decision Points

Exhibit #5: Internal Revenue Code 26 § 213 (d) Definitions.

Exhibit #6: Internal Revenue Code 26 § 152 Dependent defined

Mr. Niss said Section 1 of LCVEBA allows employees to deposit sick leave into a health care trust account, Section 2 funds the system through sick leave, and Sections 3 through 8 create the health care trust accounts.

Mr. O'Connor distributed copies of Exhibit #4.

Mr. Niss distributed copies of Exhibits #5 and #6 for Subcommittee reference.

Rep. Brainard said the use of the word "retained" in Section 6 (2) makes it sound as if the funds cannot be withdrawn from the account for any reason. Mr. Niss said the qualifier is in the next sentence. Sen. Bartlett said a more correct phrase may be "credited to." Rep. Brainard said he would accept Mr. Niss' explanation.

Rep. Brainard asked if the system would pay reimbursements only, or if a doctor's office could bill the trust account directly, because some people's cash flow may not permit them to pay the bill and then wait for reimbursement. Mr. Niss said the question is not addressed in the bill draft and will be left to the administrator's decision. He said that it depends on whether the expense that is incurred corresponds to the definition of a qualified expense.

Sen. Ekegren said there were some questions for consideration on Exhibit #4. Mr. O'Connor said those questions did not need to be answered today.

Joyce Brown, Employee Benefits Bureau, Department of Administration, said that she tried to calculate a rough estimate on the cost of the trust accounts. She said that by taking averages of the amount of sick leave accrued by current PERS employees and its average value, she would estimate the cost of funding the plan to be \$42 million.

Rep. Brainard asked if Ms. Brown had taken the 25% of sick leave as specified elsewhere in the bill. Ms. Brown said that she did not, but rather she used straight time. Rep. Brainard drew attention to an ambiguity in the draft regarding the 25% of the value of unused sick leave. Ms. Brown said the 25% reduced the estimation of cost down to approximately \$10 million.

Ms. Brown said that a VEBA is the only vehicle she knows about where the funds are pretax both going in and coming out, but the catch is that it has to be through group participation. She asked what happens to accrued funds if someone leaves the group. Would participation be mandatory for new hires? Why are there criminal offenses attached to the bill when there would be tax consequences for fraud?

Mr. Niss said whether the criminal penalties are included is up to the discretion of the Subcommittee. He said criminal penalties are important if the payments have to be made by PERS staff or, more importantly, if the plan is self-administered.

Ms. Heffelfinger said current VEBAs mandate participation of new hires and, even if the member moves to another employer, membership in the group is retained. Mr. Niss added that it is unknown to staff at this time whether or not that is an IRS qualification.

Rep. Brainard asked what would happen if a member would transfer to an employer who does not participate in the medical trust account system and requests the new employer to make deductions for account contribution. Ms. Heffelfinger said public employer participation must be authorized, so the employer would not be able to make those deductions for a new hire unless specific provision was made in the bill.

Mr. O'Connor said the medical trust accounts would be for employers in local government, too, and the cost to them must be considered. He asked if this would constitute an unfunded mandate. He said that because there are 200 employers in the PERS that have less than ten employees each, the question of their eligibility must be considered. He suggested using a percentage of employees voting for participation rather than the set number of ten.

Sen. Bartlett said she would like to require 10 employees to petition, and then a percentage of the total voting to adopt the system. Rep. Brainard said a percentage for petition could be used, too. Mr. Niss said that it must be remembered that the department, bureau, office scheme described in the bill draft may not describe the

organization of local governments. Mr. O'Connor said an undue burden may be placed on state personnel to determine eligibility because he does not believe that the PeopleSoft software that agencies use can extract that information. Mr. Niss said he chose the PERB because of its independence from both employer and employee, and said that he believes there would be serious problems if the trustee was not an independent entity.

Mr. Senn asked if the 7% PERS deduction will apply to payouts from the trust like it is on regular sick leave payout. He said he also believes the 60-hour retention of sick leave may not be adequate for maternity leave or for major surgery.

Rep. Brainard asked about the voluntary contribution of sick leave to a bank. Ms. Heffelfinger said employees can contribute to a sick leave pool within an agency. Mr. Niss said he did not add that provision to the bill because of Section 9 (IRS qualification). Ms. Heffelfinger said she did not know whether local governments have a sick leave pool like state agencies do.

Sen. Bartlett said there are many issues that need to be addressed before the bill can be put in final form. She suggested that staff create an Issues and Options paper that contains these issues.

Rep. Dell said he was not prepared to act on the bill draft at the present time because he has too many unanswered questions.

Ms. Heffelfinger said a new bill draft incorporating some of the points that need to be addressed can be written. She said some of the complications can be worked out with Ice Miller, the consultant retained by the Committee. She asked if the Subcommittee preferred to hear the bill alone, or if they would prefer to have it presented to the full committee.

Rep. Brainard said that as much as possible should be resolved within the Subcommittee. He said that one more meeting might be possible, but a conference call is a possibility, too.

Sen. Bartlett said she would prefer an Issues and Options paper, a conference call, and then a re-drafting of the bill. Rep. Brainard said he agreed.

Rep. Dell said he was very concerned about the fiscal implications for the state if the health care trust accounts were to be created. Rep. Brainard suggested a phase-in program for contribution of sick leave to establish the accounts, so the fiscal impact is spread out.

Ms. Heffelfinger asked if the policy guidelines are still current, i.e., options at the lowest level possible but participation is according to stated guidelines. Rep. Brainard said the guidelines are established through the IRS Code and enabling legislation is being written to use what is available through the IRS. He said to micro manage the system's creation may not be the best approach.

Sen. Ekegren instructed staff to proceed as discussed.

Sen. Bartlett said she remembered a discussion involving the member's use of the funds during current employment. She also reminded staff to investigate non-criminal penalties for fraud.

Ms. Brown encouraged the Subcommittee to continue to include the PERB in the discussions.

ADJOURNMENT

There being no further business to be brought before the Subcommittee, the meeting was adjourned at 12:00 noon.

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